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BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of	)	
	)	
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992	)	**MM Docket No. 92-266**
	)	
Rate Regulation	)	

REPLY TO OPPOSITIONS TO PETITIONS FOR RECONSIDERATION

Cablevision Industries Corporation
Comcast Corporation
Cox Cable Communications,
a division of Cox Communications, Inc.
Jones Intercable, Inc.
Mid-Coast Cable Television, Inc.
Service Electric Cablevision, Inc.
Vista Communications, Inc.

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The Joint Parties (listed in Appendix A hereto), by their attorneys, hereby submit their reply to oppositions to the Joint Parties' Petition for Reconsideration (the "Petition") in the above-captioned proceeding. As shown below, the Commission should grant the relief requested in the Petition.

The Commission faces a formidable task — it must adopt regulations to carry out the 1992 Cable Act and at the same time ensure that its regulations will not jeopardize the economic vitality of the cable industry. If it is to achieve these goals the Commission must adjust the benchmarks and provide cable operators with more flexibility to promptly adjust rates in response to increased costs. The positions advanced in the Oppositions to the Petitions for Reconsideration should be rejected because they are incompatible with these goals. Their acceptance would impair the ability of the cable industry to provide new and innovative services to the public at a critical stage in its development.

I. The Commission Must Act to Reduce the Burdens of Rate Regulation.

The parties which oppose corrections to the overly-restrictive rate regulations adopted in the Order base their opposition on the implicit assumption that the current rules do not discipline cable operators severely enough. The goal of the 1992 Cable Act was not, however, to punish cable operators. Where cable systems are not subject to effective competition, the Act's goal is to "ensure that consumer interests are protected." The Act also makes clear the importance of maintaining the technological and programming growth that has distinguished the cable industry.

A. Rate Regulation Must Account for the Differences Between Basic and Cable Programming Service.

The Joint Parties' Petition established that the 1992 Cable Act was intended to create a two-level regulatory scheme which distinguished between basic and cable programming service rates. Petition at 1-10. This distinction is reflected in the substantive and procedural elements of the 1992 Cable Act and from Congressional intent. Id. Based on this evidence, the Joint Parties argued that the Commission should reconsider its rate regulations and reform them to reflect different standards for the two kinds of service.

Several parties dispute this approach, arguing that Congress intended only a single kind of regulation. The statute, however, does not support their arguments. Both NATOA and King County claim that the factors to be considered in evaluating basic and cable programming service rates are very similar when there are significant differences. See, e.g., King County, et al. Opposition at 24. See generally, GTE Opposition at 2-5. As the Petition explains, only two factors among the six or seven to be considered in each instance are identical.[1/]

Second, these parties argue that the use of "reasonable" to describe permissible basic service rates and "unreasonable" to describe impermissible cable programming service rates does not connote differences in how the two services are to be regulated. NATOA Opposition at 9-10. As described in the Petition, basic principles of statutory

1/ Petition at 5. King County argues that even if the Commission considered all statutory factors, because there is great overlap, the Commission may reasonably conclude that the regulatory system governing basic and cable programming service rates should be the same. King County Opposition at 24. This analysis is flawed because the Commission did not consider all factors, and because only two of six or seven factors in fact overlap. Had the Commission followed the statutory mandate, it is more likely that there would have been different regulatory schemes. Petition at 5.

construction show that this argument is wrong. Petition at 2. This is especially the case because "reasonable" and "unreasonable" have specific meanings in the rate regulation context, a fact certainly known to Congress. Id. A regulatory scheme that does not account for these distinct terms is incurably flawed.[2]

B. More Comprehensive Recovery of External Costs Is Necessary.

Those parties that oppose more complete recovery of external costs betray fundamental misunderstandings of the nature of the regulation that is now being imposed on cable operators. First, the franchising authorities misunderstand how external cost flow-throughs operate under the benchmark/price cap scheme.

NATOA and King County argue against broadening external cost pass-throughs because cable operators would be able to "double dip." [3] Both NATOA and King County appear to believe that all external costs, present and future, somehow are incorporated into the September 30, 1992 rates, adjusted for inflation. Rather, a cable operator can only benefit from an external cost pass-through to the extent that the cost was

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2/ NATOA argues that the legislative history shows that Congress intended for the two terms to have the same meaning because the Commission is permitted to set reasonable rates for cable programming service after a complaint is filed. NATOA Opposition at 10 n.10. The legislative history actually confirms that Congress was following established principles of rate regulation, which permit a rate outside the zone of reasonableness (i.e. an unreasonable rate) to be reset to a level that is inside the zone of reasonableness (i.e. a reasonable rate). See FERC v. Pennzoil Producing, 439 U.S. 508, 517 (1979) (describing zone of reasonableness).

3/ See NATOA Opposition at 12-13. NATOA also argues that cable operators should not be permitted to recover costs of upgrades because upgrades might benefit unregulated services. Id. BellSouth makes a similar argument, apparently assuming that all upgrades are intended to benefit only non-regulated services. BellSouth Opposition at 4-6. See also Bell Atlantic Opposition at 4-5; Michigan Communities Opposition at 17. Of course, cable operators will be required to allocate upgrade costs between regulated and unregulated services, just as other external costs such as franchise fees must be allocated under the current rules. BellSouth's apparent belief that there are no "innocent" upgrades may be a reflection of its own business strategies, but that has no relevance to the behavior of cable operators or the requirements of the rules.

not part of the September 30 rate (such as a new or increased tax or fee) and that over all its external costs increase at a rate higher than inflation. In fact, the current rules unreasonably deprive cable operators of any cost recovery for external costs between September 30, 1992 and the first date of regulation. For those costs, the rules do not permit even a "single dip." Operators should be permitted to recoup these costs.[4/]

Also, the regulations must be modified so that operators can recover external costs as they are incurred, instead of annually. Currently the lag between the time that costs may be incurred and when they may be recouped is significant. For example, if above inflationary programming costs were to increase by 5 cents per subscriber on January 1, 1994, those costs should be passed on at that time. Under the rules it could take until sometime in 1995 before a system recovers costs actually incurred in January, 1994.[5/] The Commission should be concerned with the reasonableness or unreasonableness of a rate increase, not with its frequency. The decision to permit rate adjustments only once a year is of major significance to the industry. There is no persuasive reason as to why operators should be required to absorb these costs over the course of a year or more, nor is there any authority in the 1992 Cable Act which authorizes the Commission to delay an operator's right to recoup costs as they occur. The added financial burden which this

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4/ Cable operators must be allowed to recover all costs, such as taxes, franchise costs (including business license fees and other charges imposed by the municipality) and programming costs that they do not control. Additionally, as in any other business, cable operators must be assured a fair chance to earn a return on those costs. NATOA and King County argue that external cost recovery should be limited, not expanded, in order to reduce cable rates. See King County, et al. Opposition at 26-27. This argument evidences a goal of lowering rates at all costs, not a concern for establishing a fair regulatory scheme. See GTE Opposition at 12-15.

5/ Appendix B is a timeline which illustrates the months that could elapse before an operator could put into effect a general rate increase for costs incurred in 1994.

framework of regulations imposes could easily be alleviated if adjustments were permitted at least quarterly rather than on an annual basis.[6]

The telephone companies argue that expanding the range of external costs would be inconsistent with telephone company price cap regulation. See, e.g., BellSouth Opposition at 3-9; GTE Opposition at 15-16. This is true, but irrelevant. Although the same term is used to describe the telephone and cable regulatory structure, the Commission purposely adopted a different cap approach for cable to better fit the cable industry, despite earlier telephone company pleas for "parity." As a practical matter, the telephone price caps were set at levels guaranteeing specific returns on investment. The FCC's benchmark/price cap regime does not contemplate profits, let alone specific levels of returns for cable.[7] Significantly, too, the statutory regulatory schemes for the two industries and the industries themselves are different, and Congress made the affirmative decision not to regulate cable operators as common carriers.[8] Cable is more than just transmitting signals; it is a communications medium which provides content as well as transmission, with its own unique characteristics. In fashioning its regulations the Commission cannot arbitrarily impose telephone-like regulations. At the least it must

6/ The Commission also should clarify that where only GNP-PI and external cost pass-throughs are at issue, the 30-day period described in footnote 355 of the Order applies and the franchising authority should not be able to further delay rate increases. The Commission's rules should specifically incorporate this clarification and make it applicable to GNP-PI-only rate increases as well. To ensure that franchising authorities can not unfairly attempt to deny GNP-PI and external cost pass-throughs, the Commission should provide that any costs that are in dispute should be permitted to be taken and placed in escrow.

7/ Rate caps for telephone companies, unlike the caps for cable television companies, were based on an extensive regulatory history. Increased efficiencies were presumed to offset for some changes in underlying costs. There is, however, no evidence of inefficiencies in the cable industry. Additionally, with regard to programming costs, cable operators are required to pass through to subscribers any savings.

8/ For instance, telephone companies are permitted to sell customer premises equipment on an unregulated basis, with no constraints on profits, while the 1992 Cable Act requires cable equipment to be made available at cost-based prices.

adjust the regulations to comport with statutory imperatives. In particular it is explicitly required by Congress to consider the cable industry's costs when setting rates. The Commission has described its external cost flow through as fulfilling that obligation. Order at ¶ 227.

C. The Order's Approach to "Tier Neutrality" Unfairly Penalizes Cable Operators.

Several parties attempt to defend the "tier neutrality" requirements of the rules and Order. Order at ¶ 396. In King County's view, in the absence of strict tier neutrality, operators could increase rates for one tier of service without reducing rates for another or have an incentive to shift services from one tier to another. King County, et al. Opposition at 22-23. See also, NATOA Opposition at 8-10.

King County's arguments are unfounded. Contrary to what Congress intended, the tier neutrality requirement effectively prevents cable operators from lowering rates for basic service in order to create low cost or "lifeline" services, because the operator cannot recoup its costs on the higher priced tier. It also prevents operators from pricing separate tiers of cable programming services according to cost or from creating specialized tiers that appeal to particular subscribers. Modifying the tier neutrality rules to permit a cable operator to get credit for low rates on one tier when determining whether another tier is lawfully priced will solve these problems without permitting cost-shifting or encouraging service-shifting.[9]

9/ King County also appears worried that changing the tier neutrality rules will increase the administrative burden on franchising authorities. Id. at 13. Using the current proposed forms as a guide, it is likely that the change described above would add at most a few lines to any calculations that a franchising authority or the Commission must review. This would not appear to be particularly burdensome.

II. The Commission Should Permit Operators to Charge Rates for Additional Outlets that Reflect the Value of Programming to Subscribers

Both the industry and consumers of cable service would benefit if the Commission refined and readjusted several aspects of its rate regulatory scheme. One such adjustment that would give operators pricing flexibility and help to maintain low basic service rates would be to permit operators to recognize the value of programming in the charges for additional outlets. The Commission should reevaluate its conclusion that cable service to additional outlets is completely subject to cost-based regulation as a component of the equipment basket. Order at ¶ 303-07.[10/] While the 1992 Cable Act requires equipment necessary to receive basic service to be regulated on a cost-plus basis, the Cable Act does not require or suggest that the Commission should prevent operators from charging for the programming received over an additional outlet. The relevant provision discussing additional outlets is entitled "Equipment" and thus the Commission should presume that it applies only to the installation and equipment used with additional outlets.[11/] The language of Section 623(b)(3)(B) says no more than that the Commission shall regulate the rates of connections for additional televisions and any interpretation restricting recovery of other associated costs goes beyond the Congressional mandate.

The legislative history of this section speaks only to regulation of the equipment used to receive additional outlet service. The House Committee adopted the provision because it was concerned that cable operators had been leasing equipment at rates that far exceed costs. House Report at 83. The Conference Report also supports this interpretation: Section 623(b)(3) "directs the Commission to establish a formula to establish the rate for . . . connections for additional television receivers." Conference

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10/ NATOA in its opposition argues that rates for additional outlets should be established at cost. NATOA Opposition at 21.

11/ 47 U.S.C. § 543(b)(3). The service component of additional outlets is governed by Section 623(b)(1), (2) regarding rate regulation generally.

Report at 60 (emphasis added). No mention is made of prohibiting recovery for additional programming provided over additional outlets.

Additionally, commenters in this proceeding have pointed out to the Commission that these rules will effectively raise the rates of subscribers with only one connection and lower the rates of subscribers with multiple connections. There is no indication that Congress mandated a policy which will increase rates for those who can least afford it.

III. The Commission Should Permit Operators and Franchising Authorities to Enter into Rate Regulation Agreements Consistent with the 1992 Cable Act

The Joint Parties have suggested a third alternative to benchmarks and cost-of-service regulation, which also has been suggested by other commenters. Petition at 23-25. This alternative could lessen the administrative burdens for franchising authorities, operators, and the Commission. The Commission must establish procedural regulations governing basic cable service that "reduce the administrative burdens on subscribers, cable operators, franchising authorities, and the Commission." 47 U.S.C. § 543(b)(2)(A). At the same time, these regulations must ensure that basic rates are reasonable. Both goals can be achieved if operators and franchising authorities are allowed to enter agreements regulating basic cable rates when the terms of the agreements are consistent with the criteria contained in the 1992 Cable Act.

Agreements should be permitted for two compelling reasons. First, the administrative burdens on all interested parties — the Commission, cable operators, and franchising authorities — would be reduced substantially. Franchising authorities could agree with cable operators so long as the agreement was consistent with the criteria of the 1992 Cable Act. Operators will be able to avoid the costs and delays inextricably associated with cost-of-service showings and which, absent this third alternative, they could be forced to undertake. Municipalities and the Commission also would have to evaluate fewer cost-of-service showings at the basic service level. Subscribers would also obtain the benefits of upgrades and other improvements on an expedited basis.

Second, permitting side agreements also will allow franchising authorities to negotiate for upgrades and service enhancements, discounts in service offerings and options which may not now be easily obtained without extensive cost-of-service showings. Side agreements that are consistent with the rate criteria of the 1992 Cable Act should not be prohibited; they promote the ability of the Commission and franchising authorities to carry out the policies of the 1992 Cable Act in a manner which best addresses local concerns and minimizes the costs on all parties. 47 U.S.C. § 543(b)(1). This is the result that should be achieved by the Commission's rate regulation scheme.

IV. Negotiated MDU Service Contracts Should Be Permitted to Meet Competition.

In their Petition, the Joint Parties asked the Commission to modify its regulations to permit operators to negotiate individual agreements for service to multiple dwelling units ("MDUs"). The Joint Parties pointed out that otherwise operators would be unable to effectively compete with alternate service providers such as SMATV operators. Petition at 43-44. Liberty Cable argues that if operators are permitted to negotiate to provide service in an MDU, that they will engage in predatory conduct. The 1992 Cable Act's legislative history permits such agreements as long as the negotiated rates are not predatory, i.e., intended to "undercut a competitor temporarily."[12/] If individual instances of predatory pricing occur, these can be brought to the Commission's attention. In the MDU context, operators need the flexibility not to be undercut by competitors and simply to meet competition of another multichannel competitor. That would seem to offer

12/ Senate Report at 76; 138 Cong. Rec. S14248 (daily ed. Sept. 21, 1992) (Statement of Sen. Gorton). Joint Parties agree with the SMATV operator Liberty Cable that predatory pricing should be prohibited. However, MDU service rates should not be presumed to be predatory. See Liberty Cable Opposition at 5.

the public the most opportunity for a competitive market. As to existing MDU service contracts, they must be grandfathered.[13/]

V. Conclusion

For all the foregoing reasons, the Joint Parties urge the Commission to reconsider the rules in this proceeding in accordance with their Petition.

Respectfully submitted,
THE JOINT PARTIES

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13/ Absent express or implied statutory authority to the contrary, as in the case of franchise agreements, 47 U.S.C. § 543(j), the Commission may not adopt regulations that preempt existing agreements. The 1992 Cable Act's uniform pricing provision neither explicitly nor impliedly preempts existing MDU service contracts. Despite its opposition to the Joint Parties' position, Liberty Cable agrees that the Commission should "grandfather existing bulk discount contracts with MDUs to avoid changing existing MDU rates." Liberty Cable Opposition at 6 n.9. Failure to exempt existing MDU contracts would require the renegotiation of literally tens of thousands of contracts industry wide. For example, Cox Cable has in excess of 4,000 bulk contracts which potentially could be subject to renegotiation if they are not grandfathered.

APPENDIX A

Joint Parties

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Comcast Corporation
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  a division of Cox Communications, Inc.
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Vista Communications, Inc.

Annual Rate Increase Time Lines

Best Case Based on Immediate Approval By Franchise Authority

January	February	March	April	May	June	July	August	September	October	November	December	January	February
				May 15: Rate Schedule or Cost Of Service Showing Prepared Using New GNP-PI	June 1: Rate Schedule or Cost of Service Showing Filed With Franchise Authority	July 1: Rate Approved. Notice to Customers Prepared	August 1: Customers Notified of Rate Increase	Sept. 1: New Rates Billed to Customers					

Rate Schedule Increase Tolled By Franchise Authority

January	February	March	April	May	June	July	August	September	October	November	December	January	February
				May 15: Rate Schedule Prepared Using New GNP-PI	June 1: Rate Schedule Filed With Franchise Authority	July 1: Unable to Evaluate Rate Schedule. Reviewing Period Extended 90 Days			Oct 1: Rate Becomes Effective But is Subject to Refunds	Nov 1: Customers Notified of Rate Increase	Dec. 1: New Rates Billed to Customers		

Cost Of Service Increase Tolled By Franchise Authority

January	February	March	April	May	June	July	August	September	October	November	December	January	February
				May 15: Cost of Service Showing Prepared Using New GNP-PI	June 1: Cost of Service Showing Filed with Franchise Authority	July 1: Unable to Evaluate Cost of Service Showing. Reviewing Period Extended 180 Days					Dec 1: Rate Becomes Effective But is Subject to Refunds	Jan 1: Customers Notified of Rate Increase	Feb. 1: New Rates Billed to Customers

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing "Reply to Oppositions to Petitions for Reconsideration" was served this 4th day of August, 1993, by delivery thereof by first class mail, postage prepaid, to the parties on the attached list.

Wanda Clay

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